

STATE OF ILLINOIS

ILLINOIS COMMERCE COMMISSION

Illinois Commerce Commission On Its Own Motion

VS.

Commonwealth Edison Company

**Investigation of tariffs approved in
Docket No. 13-0386.**

.....

Docket No. 13-0553

INITIAL BRIEF OF THE STAFF
OF THE ILLINOIS COMMERCE COMMISSION

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and to supersede specified final orders of the Commission. Along with other new provisions, P.A. 98-15 creates Subsection 16-108.5(k)(1), which states that no earlier than five business days after the effective date, each participating utility (as defined in Section 16-108.5(b)) shall file any tariff changes necessary to implement the amendatory language and a revised revenue requirement under the participating utility's performance-based formula rate. Subsection 16-108.5(k)(1) further required the Commission enter a final order approving such tariff changes and revised revenue requirement within 21 days after the participating utility's filing.

On May 30, 2013, Commonwealth Edison Company ("ComEd") filed tariff pages and revised revenue requirements responsive to P.A. 98-15. On June 5, 2013, the Commission entered an order in Docket No. 13-0386 finding that ComEd's proposed tariff changes made on May 30, 2013 were in compliance with the recent legislation and approving the company's revenue requirement modifications.

On October 2, 2013, the Commission on its own motion, based upon a Staff report which raised questions concerning ComEd's tariff filing of May 30, 2013, and pursuant to the authority of Section 10-113(a) of the Act to rescind, alter or amend its order in Docket No. 13-0386, initiated a proceeding to determine whether the tariff changes filed by ComEd on May 30, 2013, comply with P.A. 98-15. The proceeding is to address the limited specific questions whether the tariffs filed on May 30, 2013: (1) correctly calculated interest on ComEd's reconciliation balance, (2) correctly calculated the Section 16-108.5(c)(5) return on equity ("ROE") collar, and (3) correctly reflected the appropriate tax treatment in calculating interest on the reconciliation balance in the

formula rate tariff as authorized by the Public Utilities Act. Illinois Commerce Commission, ICC Initiating Order Docket No. 13-0553, 2 (October 2, 2013).

An emergency status hearing was held on October 7, 2013, and the parties agreed to a schedule that would allow the Commission to issue an Order prior to November 30, 2013. The People of the State of Illinois, through Attorney General Lisa Madigan ("AG"), the Illinois Industrial Energy Consumers ("IIEC"), the Citizens Utility Board ("CUB"), and the City of Chicago ("City") were granted leave to Intervene. Staff witness Richard W. Bridal II submitted testimony in this case. ComEd and AG filed testimony independently, while the IIEC, City and CUB filed testimony jointly.

An evidentiary hearing was held in this matter in Chicago, Illinois on October 24, 2013. Pursuant to the direction of the Administrative Law Judges, Staff's initial brief follows.

II. PA 98-15 COMPLIANCE

- A. Do the tariffs filed on May 30, 2013 by ComEd correctly calculate interest on ComEd's reconciliation balance as authorized by the Public Utilities Act?

Staff's position is that the Commission should find that the tariffs filed on May 30, 2013 by ComEd reference revised schedules that would incorrectly reflect the calculation of interest on the reconciliation balance at the grossed up Weighted Average Cost of Capital ("WACC"). The revised schedules submitted with the tariffs filed by ComEd on May 30, 2013 are not correct and must be revised for a number of reasons. First, applying a gross up of the WACC as the rate of interest is contrary to the explicit language set forth in Section 16-108.5(d)(1) of the Act. Second, such a change to the WACC as the interest rate is not necessary, as the reconciliation balance is already the

difference between two revenue requirement amounts already grossed-up for the effect of income taxes, and as such, the interest calculated on the reconciliation balance is also already grossed up. Third, such a change to the WACC interest rate is inconsistent with Commission practice with regards to the interest rates applicable in other reconciliation proceedings. Finally, such a gross-up was not set forth in ComEd's previous schedules reflecting the calculation of the amount to be recovered from ratepayers through its formula rates in Docket Nos. 11-0721 and 12-0321. Likewise, the schedules of Ameren Illinois Company¹ ("Ameren") do not reflect a gross-up of the WACC in the calculation of the amount to be recovered through formula rates in Docket No. 13-0301. (Staff Ex. 1.0, 3-4.)

1. *Gross-up of WACC for Purposes of Calculating Interest on the Formula Rate Reconciliation Balance is Contrary to the Explicit Language of the Act*

ComEd's testimony in this proceeding is replete with incorrect statements implying that the Act allows the Company to "earn" on the reconciliation balance.² ComEd testimony is also filled with incorrect statements implying that the Act allows the Company a rate of "return" on the reconciliation balance.³ However, all of these

¹ Ameren Illinois Company is also a "participating utility" under Section 16-108.5 of the Act.

² For example, ComEd states "ComEd should earn an interest rate" (ComEd Ex. 1.0, 23), "interest earned by ComEd is taxable" (ComEd Ex. 3.0, 6), "PA 98-0015 applies interest to the reconciliation balance in a manner that allows the utilities to recover the cost of financing the reconciliation balance by *earning* its WACC" (ComEd Ex. 4.0, 6), "the interest rate participating utilities are allowed to earn is the WACC" (ComEd Ex. 4.0, 9), and "The only way to recover the cost of financing the reconciliation is to earn the WACC with the impacts of income taxes" (ComEd Ex. 4.0, 10-11).

³ For example, ComEd states "That gross up was performed for the same reason that the formula includes a gross up of WACC on the reconciliation balance: to allow ComEd the (continued...)"

statements suffer from the same infirmity: they misinterpret the explicit language within Section 16-108.5(d)(1) of the Act. Section 16-108.5(d)(1) provides for the calculation of *interest* on the reconciliation balance, and states, in part:

Any over-collection or under-collection indicated by such reconciliation shall be reflected as a credit against, or recovered as an additional charge to, respectively, with interest calculated at a rate equal to the utility's weighted average cost of capital approved by the Commission for the prior rate year, the charges for the applicable rate year.

220 ILCS 5/16-108.5(d)(1). The Act does not provide for *earnings* or *return* on the reconciliation balance. Rather, the Act explicitly provides for the calculation of *interest* at a prescribed interest rate. That interest rate is simply the WACC, as defined by the statute. ComEd itself acknowledges this fact, stating “After PA 98-0015 became law, the **interest rate** used to reflect the carrying costs (i.e., the time value of money) applicable to the delay in receiving (or refunding) the reconciliation adjustment **is ComEd’s weighted average cost of capital (“WACC”).**” (ComEd Ex. 1.0, 13 (emphasis added).)

When interpreting a statute, the primary objective is to ascertain and give effect to the intent of the legislature. Metro Utility Co. at 274. The best indication of what the legislature intended is the statutory language itself. Id. Clear and unambiguous terms are to be given their plain and ordinary meaning (West Suburban Bank at 507) and

(continued from previous page)

opportunity to recover its tax costs and the opportunity to end up recovering the return allowed by the statute” (ComEd Ex. 2.0, 4:74-77), “I am not aware that the Commission has ever disallowed this gross up, no doubt because they all recognize a utility cannot earn the authorized return without it. The gross up of the WACC interest on the reconciliation balance is no different” (ComEd Ex. 1.0, 16), “It is exactly analogous to the return on rate base gross up I just mentioned” (ComEd Ex. 1.0, 18), and “Just as the return on rate base must be grossed up, so must the WACC interest” (ComEd Ex. 1.0, 19).

where statutory provisions are clear and unambiguous, the plain language as written must be given effect, without reading into it exceptions, limitations, or conditions the legislature did not express. Davis at 184-185.⁴ The Act requires that any reconciliation over or under collection be refunded or recovered as an additional credit or charge “with interest calculated at a rate equal to the utility’s weighted average cost of capital approved by the Commission for the prior rate year.” 220 ILCS 5/16-108.5(d)(1). Section 16-108.5(d)(1) of the Act does not provide for adjusting WACC for the purported impact of income taxes. Neither the original language of Public Act 97-0616, the updated language of PA 97-0646, nor the updated language of PA 98-0015 (which was passed specifically to clarify the law on multiple contested formula rate issues, including the issue of the appropriate reconciliation interest rate) mention any type of adjustment or gross-up to the WACC interest rate for the purported impact of income taxes. Further still, the issue of adjusting the interest rate for the purported impact of income taxes appears to be some new idea of ComEd witness Brinkman, since it was never mentioned in the testimonies of ComEd witnesses Mr. Hemphill or Ms. Houtsma in Docket No. 11-0721,⁵ nor ComEd witnesses Mr. Hemphill or Ms. Houtsma in Docket

⁴ Though the language of Section 16-108.5(d) is clear and unambiguous, the Commission need look no further than the Senate transcript of the day Public Act 98-15 was passed to emphasize how clear the language is this Section of the Act now is:

SENATOR HARMON: Thank you, Mr. President. One last question. Is it correct that the Illinois Commerce Commission has seen this language and agrees it is clear and unambiguous? ...SENATOR J. CULLERTON: Yes. The Illinois Commerce Commission was provided with drafts of the legislation. At its request, a number of changes were made to clarify language that they did not believe was completely clear. With those changes which, with this bill, are part of the legislation, the ICC has represented that it is in agreement that the language of the bill is clear and unambiguous. (Tr., 98th General Assembly, March 14, 2013, 14.)

⁵ See, Commonwealth Edison Co., ICC Docket No. 11-0721, ComEd Ex. Nos. 1.0 and 4.0 generally, ComEd Ex. 12.0 at 35-37, and ComEd Ex. 21.0 at 24-29.

No. 12-0321.⁶ Although Company witness Mr. Fruehe claims ComEd has long been aware of the need to recover tax costs due to the gross-up of the equity return component for purposes of calculating an overall return on rate base, he admits ComEd did not include such a gross-up to the WACC interest rate for the purported impact of income taxes until after Public Act 98-0015 became law, calling the omission of the gross-up an “oversight.” (ComEd Ex. 2.0, 3-4.) Finally, Staff notes that Ameren Illinois Company, which is operating under the same formula rate legislation as ComEd, has not interpreted the PUA to allow the gross up of the WACC for purposes of calculating interest on the reconciliation balance. (Staff Ex. 1.0, 6.)

2. Gross-up of WACC for Purposes of Calculating Interest on the Formula Rate Reconciliation Balance is Not Necessary From an Accounting Perspective

By definition, the reconciliation balance is the difference between two revenue requirements, and each of those revenue requirements was already grossed-up for income tax that was either expected to be paid or actually paid by the utility. Thus, the reconciliation balance itself is already grossed-up for taxes. This fact is not disputed. (ComEd Ex. 3.0, 8.) Thus, logically, the interest on the reconciliation balance, which is calculated by multiplying the statutorily provided WACC interest rate by the reconciliation balance (which, as stated above is already the difference between two grossed-up amounts), is also already grossed-up for taxes. (Tr. 14:13-24, Oct. 24, 2013.) To gross-up that interest amount for taxes again would give the Company

⁶ See, Commonwealth Edison Co., ICC Docket No. 12-0321, ComEd Ex. No. 1.0 generally, ComEd Ex. 2.0 at 10-11, and ComEd Ex. 21.0 at 24-29.

additional compensation for the income taxes ComEd anticipates will be paid on the compensation ComEd will receive for the time value of money. (Staff Ex. 2.0, 2.)

3. *Gross-up of WACC for Purposes of Calculating Interest on the Formula Rate Reconciliation Balance is Not Consistent with Commission Practice*

With regards to the Commission's orders in other reconciliation proceedings, the Commission has not and does not gross-up interest associated with the reconciliation balance. (Staff Ex. 1.0, 4.) While non-formula rate reconciliations may not involve the reconciliation of the *full* cost of providing distribution service provided by the formula rate law, non-formula rate reconciliations nonetheless provide for the reconciliation of at least one component of that distribution service cost. (Staff Ex. 1.0, 4-5; ComEd Ex. 3.0, 8.) The Water/Sewer Qualified Infrastructure Plant Surcharge ("QIPS") provided for in 83 Ill. Adm. Code Part 656 is the most similar to the formula rates, as it provides for a return on and a return of plant investments in a similar manner as the formula rate revenue requirement. Even so, the Commission has not previously grossed-up the interest associated with the QIPS reconciliation. (Staff Ex. 1.0, 4-5.)

The Company attempts to draw a distinction between the formula rate reconciliation balance and the reconciliation balances resulting from other, non-formula rate reconciliations where none exists. (ComEd Ex. 3.0, 8-9.) Both formula rate and non-formula rate reconciliations result in the same type of reconciliation balance – an under-recovery or an over-recovery of costs associated with distribution services. (Staff Ex. 3.0, 5.) Further, both formula rate and non-formula rate reconciliations involve the calculation of interest using an interest rate provided for by law or administrative rule.

(Staff Ex. 3.0, 3; see e.g. 220 ILCS 5/16-108.5(d)(1), 83 Ill. Adm. Code 656.80(i).) As such, and contrary to the Company's claims, the reconciliations are fundamentally similar. Consistent with Commission practice with regards to interest rates applicable in other distribution cost reconciliations, the WACC interest rate associated with the formula rate reconciliation should not be grossed-up for income taxes.

4. The Gross-Up in the Interest Rate was Not Reflected in ComEd's Previous Schedules and Ameren Does Not Gross-Up Its WACC

Finally, ComEd filed schedules in Docket Nos. 11-0721 and 12-0321 which did not reflect a gross-up of the interest rate applied to the reconciliation balance. As stated above, and as ComEd witness Brinkman confirms, even though ComEd requested the interest rate applied to the reconciliation balance be the WACC, at no time did ComEd request the Commission to gross-up the WACC for income taxes. (Staff Ex. 1.0, 3-4; Tr. 66:10-15, October 24, 2013.) It was only after the passage of P.A. 98-15 that ComEd suddenly decided that WACC should include a gross-up. Strangely, ComEd calls this an "oversight." (ComEd Ex. 2.0, 3-4.) However, ComEd advocated for the WACC to be applied to the reconciliation balance in Docket Nos. 11-0721 and 12-0321 and made no mention of a required gross-up.

Ameren is also a participating utility as is defined by Section 16-108.5 of the Act. Like ComEd, Ameren is undergoing its formula rate update case at this time in Docket No. 13-0301. (Staff Ex. 1.0, 3-4.). Unlike ComEd, Ameren did not apply a gross-up to its WACC interest rate. Ms. Brinkman confirmed this. (Tr. 24:42, Oct. 24, 2013.) Clearly, Ameren does not find it necessary to gross-up the interest rate applied to the reconciliation balance to make itself whole and has correctly interpreted the plain language of P.A. 98-15.

- B. Do the tariffs filed on May 30, 2013 by ComEd correctly calculate the Section 16-108.5(c)(5) return on equity ("ROE") collar as authorized by the Public Utilities Act?

Staff's position is that the tariffs filed on May 30, 2013 by ComEd reference revised schedules that would correctly calculate the return on equity ("ROE") collar as authorized by the Section 16-108.5(c)(5) of the Act. Staff cannot support the proposal made by Mr. Effron (AG Ex. 2.0, 3-7) to use average rate base for purposes of the ROE collar calculation. The proposal, regardless of its merits, should be rejected because, although the Act does not specifically prescribe use of either average or year-end rate base for purposes of the ROE calculation, year-end rate base is the only rate base specifically prescribed elsewhere in Section 16-108.5 of the Act.

In describing the ROE collar calculation, Section 16-108.5(c)(5) of the Act states, in part:

If the participating utility's earned rate of return on common equity ... (calculated using costs and capital structure approved by the Commission as provided in subparagraph (2) of this subsection (c)), consistent with this Section, in accordance with Commission rules and orders, including, but not limited to, adjustments for goodwill, and after any Commission-ordered disallowances and taxes) [...].

220 ILCS 5/16-108.5(c)(5) (emphasis added).

After revision by Public Act 98-0015, Section 16-108.5(c)(2) of the Act states in part that the performance-based formula rate shall:

reflect the utility's actual year-end capital structure for the applicable calendar year, excluding goodwill, subject to a determination of prudence and reasonableness consistent with Commission practice and law.

220 ILCS 5/16-108.5(c)(2) (emphasis added).

Following revision by Public Act 98-0015, Section 16-108.5(d)(1) of the Act also requires use of a year-end rate base for *reconciliation purposes*, concluding subparagraph (1) stating in part:

Notwithstanding anything that may be to the contrary, the intent of the reconciliation is to ultimately reconcile the revenue requirement reflected in rates for each calendar year, beginning with the calendar year in which the utility files its performance-based formula rate tariff pursuant to subsection (c) of this Section, with what the revenue requirement determined using a year-end rate base for the applicable calendar year would have been had the actual cost information for the applicable calendar year been available at the filing date.

220 ILCS 5/16-108.5(d)(1) (emphasis added).

While the Act does not specifically prescribe use of either average or year-end rate base for purposes of the ROE collar calculation, it is well established in Illinois that related statutes should be construed in a harmonious manner and in a manner that advances, not defeats, the legislative intent. Knolls Condominium Ass'n v. Harms, 202 Ill.2d 450, 458 (2002). Year-end rate base is the only rate base specifically prescribed elsewhere in Section 16-108.5 of the Act. 220 ILCS 5/16-108.5.

The Act is clear that year-end capital structure must be used for purposes of the ROE calculation. 220 ILCS 5/16-108.5(c)(5). However, because the Act does not specifically prescribe use of either average or year-end rate base for purposes of the ROE calculation and because year-end rate base is the only rate base specifically prescribed elsewhere in Section 16-108.5 of the Act, Staff concludes that use of year-end rate base to calculate the ROE collar is most consistent with the Act.

- C. Do the tariffs filed on May 30, 2013 by ComEd correctly reflect the appropriate tax treatments in calculating interest on the reconciliation balance in the formula rate tariff as authorized by the Public Utilities Act?

Staff's position is that the tariffs filed on May 30, 2013 by ComEd reference revised schedules that would correctly present ComEd's reconciliation balance that would be subject to a calculation for interest as authorized by the Section 16-108.5(d)(1) of the Public Utilities Act ("Act"). Staff cannot support the proposal made by Mr. Brosch (AG Ex. 1.0, 9-17), Mr. Effron (AG Ex. 2.0, 7-11), and Mr. Gorman (CCI Ex. 1.2, 6-8) to net Accumulated Deferred Income Tax ("ADIT") related to the reconciliation balance before calculating interest. The proposal, regardless of its merits, should be rejected because the Act, in particular Section 16-108.5(d)(1), does not state that the reconciliation amount is to be reduced by ADIT. Section 16-108.5(d)(1) provides in part that:

Any over-collection or under-collection indicated by such reconciliation shall be reflected as a credit against, or recovered as an additional charge to, respectively, with interest calculated at a rate equal to the utility's weighted average cost of capital approved by the Commission for the prior rate year, the charges for the applicable rate year.

220 ILCS 5/16-108.5(d)(1).

When interpreting a statute, the primary objective is to ascertain and give effect to the intent of the legislature. Metro Utility Co. v. Illinois Commerce Commission, 262 Ill.App.3d 266, 274 (1994). The best indication of what the legislature intended is the statutory language itself. Id. Clear and unambiguous terms are to be given their plain and ordinary meaning (West Suburban Bank v. Attorneys Title Insurance Fund, Inc., 326 Ill.App.3d 502, 507 (2001)) and where statutory provisions are clear and unambiguous, the plain language as written must be given effect, without reading into it exceptions, limitations, or conditions the legislature did not express. Davis v. Toshiba Machine Co., 186 Ill.2d 181, 184-185 (1999). The Act requires that any reconciliation

over or under collection be refunded or recovered with interest. 220 ILCS 5/16-108.5(d)(1). The phrase “[a]ny over-collection or under-collection” refers to the whole reconciliation balance and not some derivative thereof. Again, there is no language in Section 16-08.5(d)(1) providing for ADIT to reduce the reconciliation balance.

III. IMPLEMENTATION OF RATE FORMULA CHANGES, IF ANY

ComEd argues that, should the Commission determine a change in the rate formula is required, that determination should be implemented both prospectively and retrospectively. ComEd states:

Because PA 98-0015 changes the rates both prospectively and retrospectively, the Commission’s interpretation of the law should also be given effect both prospectively and retrospectively. Otherwise, ComEd’s net revenue requirement and rates, both in 2014 and in years before, will be based on a revenue requirement calculation that the Commission now disavows and that PA 98-0015 directed the Commission to correct. Therefore, if any change is made to the rate formula, ComEd should calculate, in its compliance filing in response to this docket, the effect on all EIMA rate years and pass through that cumulative adjustment in 2014, in a manner equivalent to how ComEd’s (sic) passed through in 2013 the adjustment required by PA 98-0015 as it was originally interpreted by the Commission.

(ComEd Ex. 3.0, 18.) Staff agrees that, should the Commission determine any changes to the formula are required, that determination should be given effect both prospectively and retrospectively. AG witness Effron opined that this matter is best left to the attorneys, however he stated that he did not mean to imply in prior testimony that any approved changes should exclude the retroactive effect of such changes. (AG Ex. 6.0, 2.)

IV. CONCLUSION

WHEREFORE, for all of the following reasons, Staff respectfully requests that the Commission's order in this proceeding reflect all of Staff's recommendations.

Respectfully submitted,

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